

Overview of Vermont's Education Funding System Under Act 68 & Act 130

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Overview of General Education Funding Under Act 68 of 2003

This overview of Vermont's education funding system is intended to describe the basic process of Vermont's education funding system. There are many technical details in the law that go beyond the scope of this presentation.

Under Act 68, Vermont's new education funding law adopted in 2003, each district will receive from the state's **education fund** categorical grants, and the total amount of its "education spending." These amounts will total more than \$1 billion.

- For funding purposes districts are town, city, and incorporated school districts.
- Union districts will not be included until FY 2007 when Act 130 of 2004 takes effect. They are currently funded by assessments to member town school districts.

What Are State Categorical Grants?

State categorical grants are separate grants distributed for specific purposes in certain spending categories. Examples of Vermont's categorical grants for FY07 are listed below:

Special Education Aid (about 60% of eligible special education)	\$125,000,000
Transportation Aid. (about 48% of transportation expenditures)	\$14,000,000
Small School Grants	\$5,000,000
Aid for State Placed Students	\$14,000,000
Technical Education Aid	\$11,000,000
Essential Early Education Aid	\$5,000,000
Total	\$174,000,000

What Is "Education Spending"?

Act 68 now pays for all of a district's education spending. How is this amount determined? Education spending is that part of an expenditure budget without a specific funding source. It includes the portion of special education costs not covered by federal aid and the state categorical grant, transportation costs not covered by the state categorical aid, as well as any tuition owed by the district, general payroll and operation costs that do not have specific funding sources. See 16 VSA § 4001(6) for the legal definition. Operationally it is determined as shown below.

Budget adopted by town, city, or incorporated school district
 + Union school assessment (if any)
 + Deficit from prior year (if any)
 Total PreK – 12 Budgeted Expenditures

Total PreK – 12 Budgeted Expenditures
 – State categorical grants, federal revenues, tuition revenues, interest income, etc.
Education Spending

In FY 2007, education spending statewide is about \$1.02 billion or 83% of total education spending.

How Is Education Fund Money Raised?

The amount needed in the education fund to pay for categorical grants and education spending is about **\$1.2 billion** in FY 2007. Revenues estimates for the education fund sources are given below.

• Nonresidential Education Property Tax	\$449 million
• General Fund Transfer	\$269 million
• One-third Sales & Use Tax	\$113 million
• One-third Purchase & Use Tax	\$27 million
• State Lottery	\$22 million
• Medicaid Reimbursement	\$9 million
• Vermont Yankee	\$2 million
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Total raised	\$891 million

Where's the Missing Money? The Variable Homestead Property Tax Rate

The amount raised above is shy of the 1.2 billion dollars needed to pay school districts. One significant revenue source has been left out. All of the above revenue sources are raised through a fixed tax rate throughout the state applied to the indicated tax base. The source left off the above list is the homestead property tax. This tax provides the balance of the funding, about \$312 million. Its rate varies proportionally with a district's education spending per pupil. The pupil count used in this determination is called the "equalized pupil" count and uses weighting for different types of pupils. The details of the equalized pupil count are discussed in a separate paper.

What is a Homestead?

32 VSA § 5401(7) provides the legal definition of a homestead. The basic components are given below.

- "[T]he principal dwelling owned and occupied by a resident individual..."
- Includes, "parcel of land surrounding the dwelling...."
- "[D]etermined without regard to any road which intersects the land."

How Are Homestead Tax Rates Determined?

A district's education spending is first divided by its equalized pupil count to determine the district's education spending per equalized pupil. This amount is compared to the state's base education spending amount per pupil to determine the percent variance. The base amount is set each year by the legislature and is \$7,330 in FY 2007.

For example, if in FY 2007, a district's education spending per pupil is \$8,063, its spending per pupil would be ten percent greater than the \$7,333 base amount. The base homestead tax rate is then increased by the same percentage or ten percent in this case. Homestead property tax rates can not be lower than the base rate even if the district spends less than the base amount. All

districts that have the same education spending per equalized pupil will have the same homestead tax rate.

Most homestead tax payers can get all or a large portion of their homestead property taxes adjusted so that the taxes are more reflective of income rather than property value.

What Are Homestead Tax Adjustments? (Prebates or Income sensitivity)

The homestead tax for eligible payers will be reduced by an amount equal to the following:

- A. If household income is \$90,000 or more, the property tax on the first \$200,000 of housesite market value (house and up to two surrounding acres) minus the applicable percentage of the household income.
- B. If household income is less than \$90,000 the homestead tax on the housesite minus the applicable percentage of the household income. An additional reduction of \$10 per acre for up to five acres beyond the housesite's two acres will also be made.

The applicable percentage of household income starts at 1.80% in FY 2007 and increases proportionally by the amount education spending per pupil exceeds the base amount the same way the homestead property tax rate increases. Beginning in the fall of 2007, adjustments determined based on prior year income and homestead tax will be made on an individual's property tax bill. This means prebate checks will no longer be distributed, rather tax bills will be reduced directly by the adjustment amount.

Homestead Tax Rate Examples

The table below shows examples of tax rates using a \$7,330 education spending per equalized pupil base amount. For FY 2007, the base homestead rates are 1.80 % of household income and \$0.95 per \$100 of homestead market value.

Education Spending per Equalized Pupil	Percent of Household Income	Homestead Property Tax Rate
(Base) \$7,330	1.80%	0.95
\$8,063	1.98%	1.05
\$8,796	2.16%	1.14
\$9,529	2.34%	1.24
\$10,262	2.52%	1.33
\$10,995	2.70%	1.43

What is Nonresidential Property and How Is This Tax Raised?

Nonresidential property is any property that is not a homestead with certain exceptions. See 32 VSA 5401(10) for statutory definition.

The property tax rate for all nonresidential property in the state is set in 32 VSA § 5402(a)(1). This rate is \$1.59 for each \$100 of fair market value.

What are the Annual Adjustments to Statutory Tax Rates?

Each December 1 the Tax Commissioner recommends adjustments to the \$1.59 nonresidential tax rate and the \$1.10 homestead tax rate based on the following:

- Projection of the amount in the education fund reserve, and
- The nonresidential rate must produce at least 34 percent of education fund spending.

For FY 2007 the nonresidential tax rate is \$1.44 and the base homestead tax rate is \$0.95.

Does the Law Limit Education Spending?

Districts with education spending per equalized pupil exceeding a prescribed amount, the threshold, will be subject to an additional tax rate. This is one of the provisions made to help limit education spending. The additional rate will be determined by adding to the district's education spending per pupil the amount that education spending per pupil exceeds the limit.

FY 07 Threshold = 25% above average education spending per pupil of prior year

The spending threshold for a school district is determined by first deducting any capital construction debt service spending.

Excess Spending Example

In FY 2007 the limit is \$11,728 per equalized pupil. The illustration below shows the tax rate that would result both without and with the limit for a district with education spending per pupil of \$12,028 using a base payment of \$7,330 and base rate of \$0.95.

	Threshold	Education Spending per Equalized Pupil	Added Penalty Amount	New Amount Per pupil	Tax Rate
Example Without Penalty	0	\$12,028	0	\$12,028	1.56
Example With Penalty	\$11,728	\$12,028	\$300	\$12,328	1.60

What Is CLA and How Is It Used?

The CLA or **common level of appraisal** for each town is determined each year by the tax department's division of property valuation and review (PV & R). PV & R compares property values listed by a town in various categories to actual sales data for each particular type of property. Using actual sales data and statistical analysis PV&R determines how close a town's grand list is compared to what it would be if all properties were listed at 100% of fair market value. It expresses this CLA as a percentage.

To ensure that state education property taxes are all assessed on the same basis, the tax commissioner is directed by law to set the tax rates in each municipality (see 32 VSA § 5402) by dividing tax rates for nonresidents and homesteads by the municipality's CLA. For example, if the education spending per pupil in a district for FY 2007 is \$8,796, the homestead tax rate from the table above would be \$1.14. If the CLA in that town was determined to be 85%, it would indicate that the town's grand list was 85% of market value instead of 100%. The tax commissioner would divide \$1.14 by 85% and get a tax rate for that town of 1.34 to adjust for the variance.

All towns that have the same education spending per pupil with the same CLA would have the same tax rate appearing on the tax bills. More likely, even if per pupil spending amounts were the same in two towns, the CLA for each would not be the same and the tax rates on the tax bills would be different.

What is Act 130, Union School Funding?

Until FY 2007 union school districts will not be recognized in Chapter 133 of Title 16, the education funding chapter. This means that until then union school districts will not receive state aid, will not have a cost per equalized pupil and will not have a tax rate. To receive funding, these districts assess costs to member town districts. The homestead tax rate then is a combination of the town district budget and the union district assessment. Union school budgets are determined by a district vote either using Australian ballot or floor vote at the union district annual budget meeting.

This has led to some confusion because two or even three school boards are responsible for one cost per equalized pupil and it has been next to impossible to break out the components. Put another way. It is hard to tell who's doing what to whom? Also, the law currently permits union schools to assess costs to member town districts using any number of apportionment methods while funding has been provided on an equalized pupil basis. This has resulted in some members of the union being overcharged while others were under charged.

Under Act 68, union districts will be recognized in the funding law and will determine an education spending per equalized pupil amount and a corresponding homestead tax rate. These districts will no longer assess costs to member districts but will receive money from the state's education fund as do the town and city school districts.

To understand how Act 130 works it is necessary to understand the distinction between governing entities. Towns or cities raise the homestead property tax on behalf of the state. These are taxing entities. School districts, town or union districts, are educating entities and do not raise

taxes. The homestead tax rate levied by a town will be based on the average education spending per equalized pupil of all the pupils living in the taxing entity.

In a K-12 district such as Rochester, all of the students in the taxing entity (the town) are members of just one school district. In a town associated with a town district and a union district, some of the pupils living in the town (the taxing entity) are members of the town school district and some are members of the union school district. The tax rate for the taxing entity (the town) will be the average tax rate (weighted average) of both districts.

If 60% of the pupils living in the town of Shelburne are members of the Shelburne town school district, and the tax rate determined for that school district is \$1.40 then 60% of that rate would be applied by the town of Shelburne or \$0.84. If 40% of the students were members of the union district and its tax rate was \$1.50, then 40% of \$1.50 or \$0.60 would be applied by the town of Shelburne. The total tax rate for the town of Shelburne would be \$0.84 + \$0.60 or \$1.44.

60% x \$1.40 (elementary district rate)	=	\$0.84
40% x \$1.50 (union district rate)	=	\$0.60
<u>Shelburne homestead equalized tax rate</u>	=	<u>\$1.44</u>